

ECONOMIC REPORT

OCTOBER 2018

Prepared for Commerce National Bank & Trust

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Disclaimer: All information in this report is for general information and educational purposes only, and should not be taken as financial/investment advice.

RECAP: LATE 2017 & THE NEW YEAR, 2018

Previously:

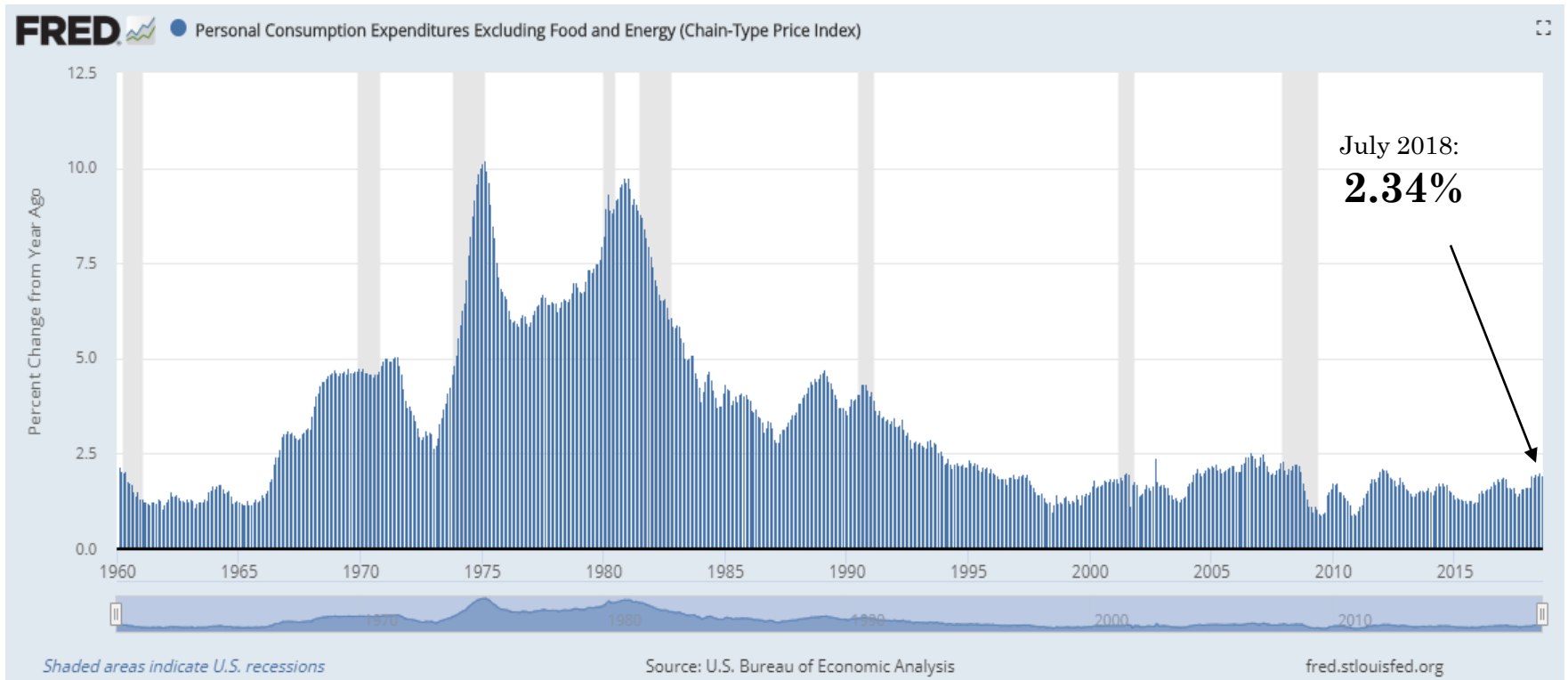
- In December 2017, President Donald Trump enacted a fiscal stimulus in the form of a \$1.5 trillion tax cut, reducing the corporate tax rate from 35% to 21%.
- In February 2018, President Trump signed a \$300 billion federal spending bill, further increasing the federal budget deficit.
- Stocks rallied through the end of 2017 and into January of 2018 in response to the tax cut. However, volatility returned to the markets in February due to investor concerns regarding inflation, rising interest rates, and potential trade wars.
- By 5/24/2018, both the S&P 500 and the Dow Jones Industrial Average had posted small losses (-1.0% and -2.2% respectively), while the Russell 2000 and NASDAQ were higher slightly by 0.4% and 2.4% respectively.

RECENT DEVELOPMENTS (2018)

- Helping to ease trade war fears, the U.S. reached bilateral trade agreements with Mexico and Canada to replace NAFTA.
- A deal has yet to be reached with China. So far, the U.S. has imposed \$250 billion worth of tariffs on China, prompting China to retaliate.
- The markets rallied again in Quarter 2, 2018 on stellar corporate earnings and new trade agreements, pushing the S&P500, NASDAQ, and DOW to new all-time highs.
- Much of 2018's gains were erased in October's first two weeks of trading due to resurfacing fears of rising interest rates and a slowdown in global growth. However, U.S. monetary policy remains accommodative – for now.
- The current economic expansion has entered its 112th month, making it the 2nd longest expansionary period in U.S. history (As of October, 2018).
- Given the rather slow economic recovery from 2010 to 2016, among reliable indicators of strength, this expansion will likely extend through 2019, becoming the longest on record.

INFLATION: PCE DEFLATOR INDEX

- The PCE Deflator Index (shown below) is the Fed's core measure of inflation.
- The index measures personal consumption expenditures over a broad range of goods and services.
- A sudden rise in inflation well above the Fed's 2% target may indicate the economy is "overheating".
 - Historical examples:
 - early 1987 – late 1990
 - early 1998 – early 2000
 - mid 2004 – mid 2005
 - late 2006 – mid 2008

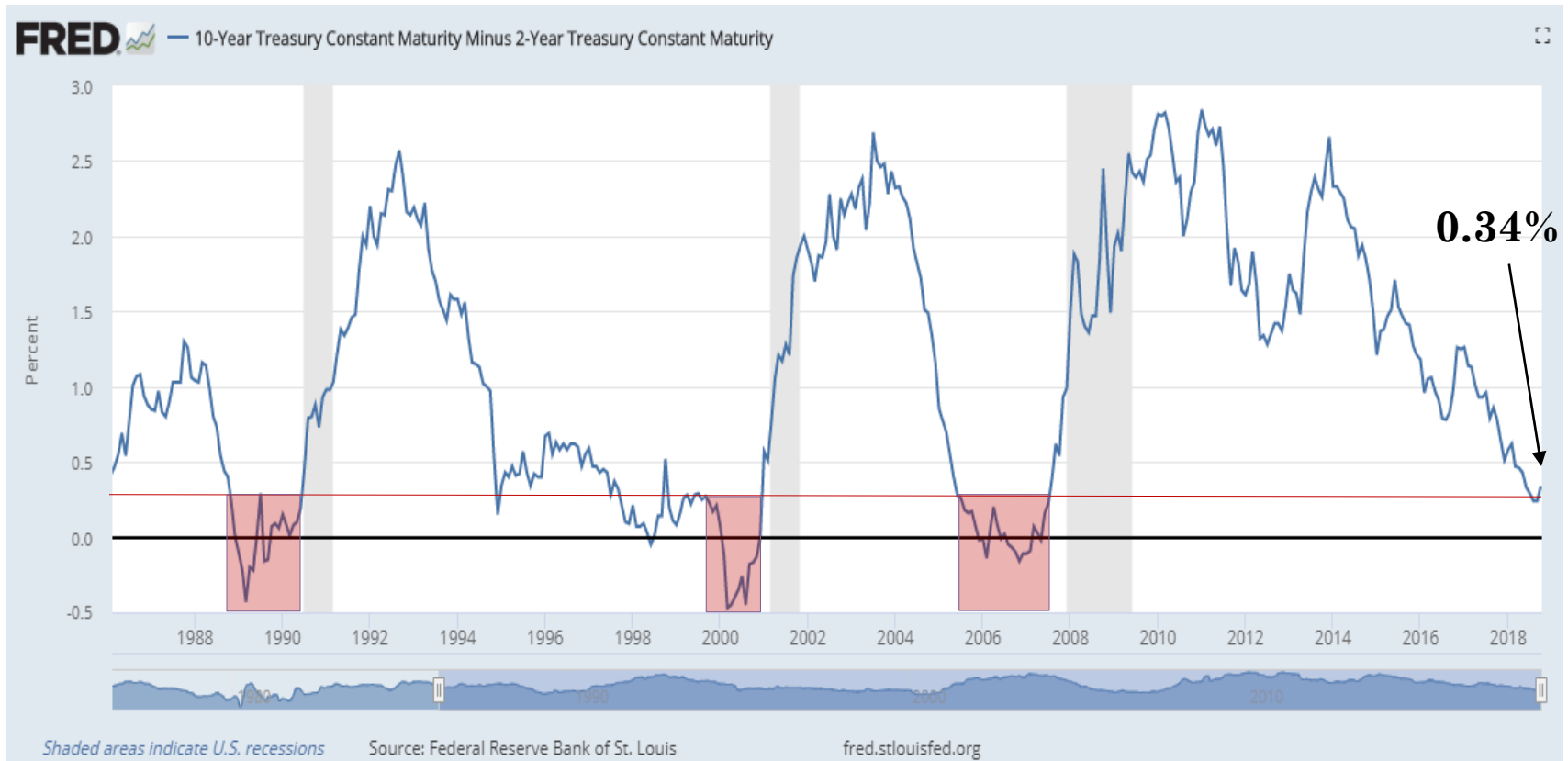


****Shaded areas indicate recessions**

Updated: October, 2018

10-2 YIELD SPREAD: OCTOBER, 2018

NOTE: If the spread falls below 0.25% (horizontal red line), a recession is expected in 2-3 years.



An inverted yield spread has preceded the past five recessions.

<https://tinyurl.com/y7o54uje>

U.S. recessions are shaded in the chart above.

Currently - 0.34%
(10/12/2018)

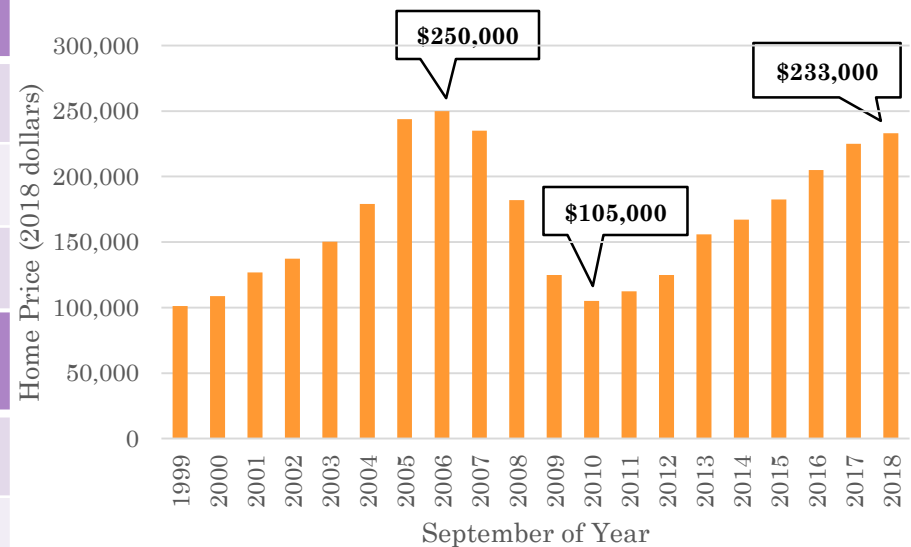
OUR 2018 HOUSING MARKET (1/5): NOMINAL PRICES, INVENTORY, BUILDER CONFIDENCE

- Prices for September 2018 were up 3.6% compared to September 2017.
- At 2.92 months supply, inventory remains very low in the Orlando market.
- Supply is especially tight for homes that are priced under \$300,000.

	Change 2017- 2018	Sep 2018	Sep 2017	Sep 2016
Median Home Price	+ 3.6%	\$233,000	\$225,000	\$205,000
Inventory (months supply)	- 14.1%	2.92	3.4	3.35
Home Builder Confidence	+ 6.2%	69	65	68
	Change 2007- 2008	Apr 2008	Apr 2007	Apr 2006
Median Home Price	- 12.8%	\$211,000	\$242,100	\$249,000
Inventory (months supply)	+ 29.4%	20.66	15.97	6.5
Home Builder Confidence	- 35.14%	24	37	57

The "Change" column shows increases/decreases over the past year.

Median Home Prices in Orlando
Nominal 1998-2018

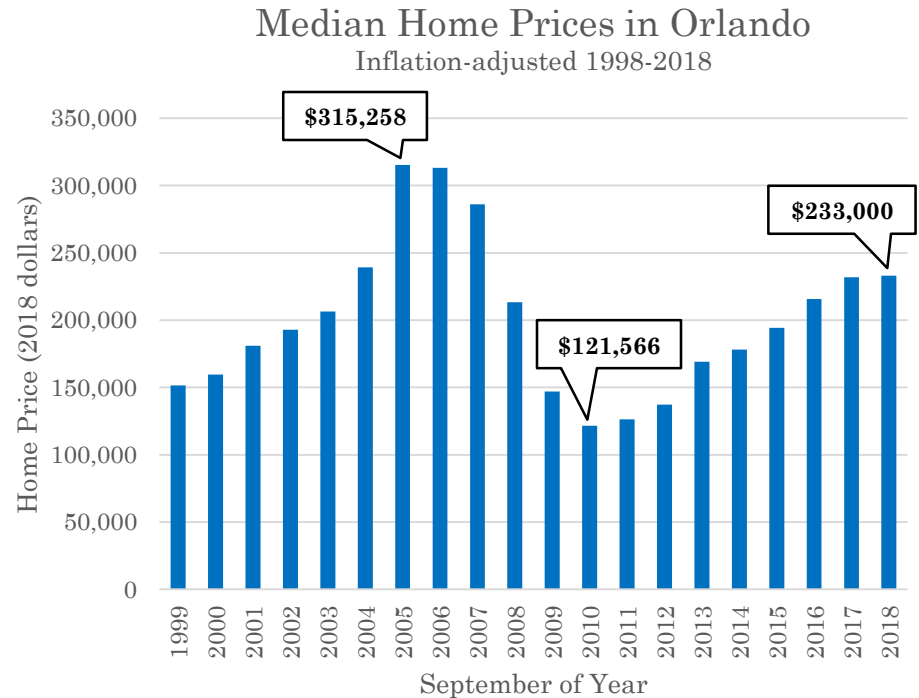


source: ORRA

Last update: October, 2018

OUR 2018 HOUSING MARKET (2/5): INFLATION-ADJUSTED PRICES - 2018 DOLLARS

- The graph: inflation-adjusted home values for Orlando (In 2018 dollars).
- Today's prices are comparable to those of 2004.
- Adjusted for inflation, today's home prices are 26% below their 2005 peak.
- Since July of 2011, the ORRA has reported year-over-year increases in median home values (an 86 month streak).
- Among other factors, we will continue to monitor prices to determine our place in the current real estate cycle.
- In August and September, year-over-year home price increases had declined to the slowest pace since 2011.
- Prices are often a lagging indicator – we are more interested in inventory, home builder confidence, and home affordability, among other indicators.

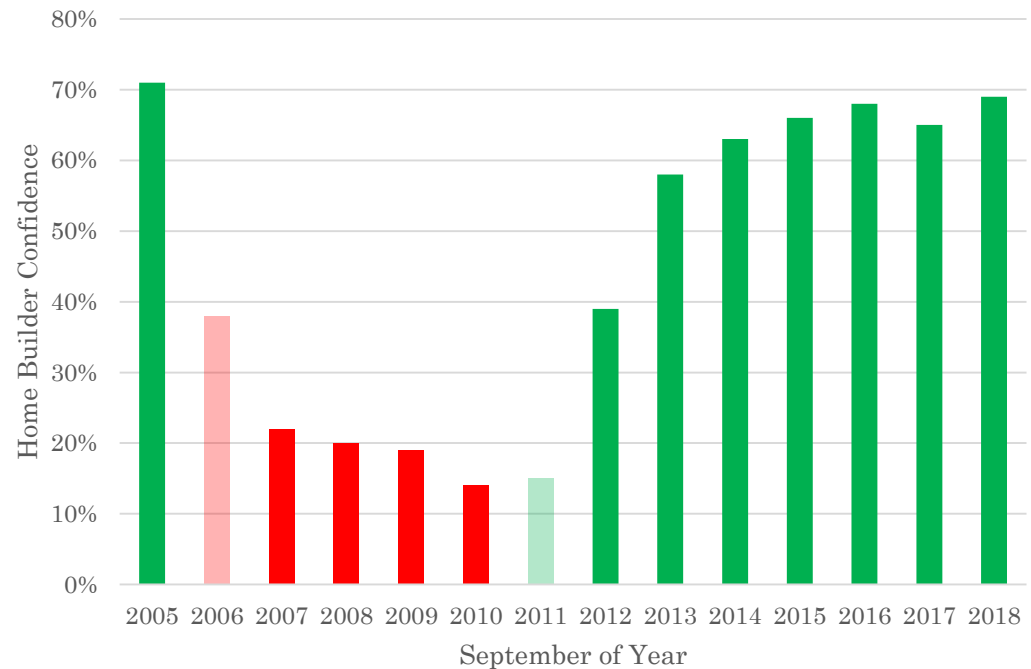


The above prices are adjusted for inflation.
source: My Florida MLS
Last update: October, 2018

OUR 2018 HOUSING MARKET (3/5): NATIONAL BUILDER CONFIDENCE

- Based on 400 survey responses from NAHB members.
- Respondents asked to rate the current market conditions:
 - Sale of new homes
 - Prospective buyer traffic
- Responses formulated into a confidence scale of 0 to 100.
- Rising confidence indicates an improving seller's market, as well as expansion in the construction cycle.
- A large decline in regional home builder confidence will occur in just a few months after the next peak in our housing market.

NAHB's Housing Market Index - South Region



<https://www.nahb.org/en/research/housing-economics>

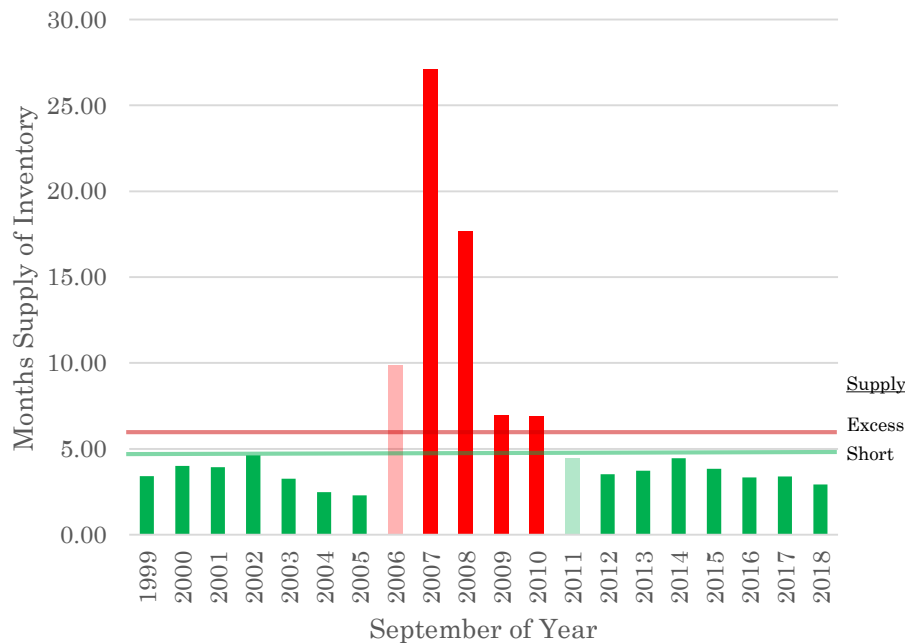
Last update: October, 2018

OUR 2018 HOUSING MARKET (4/5): REAL ESTATE INVENTORY VS. REAL PRICES

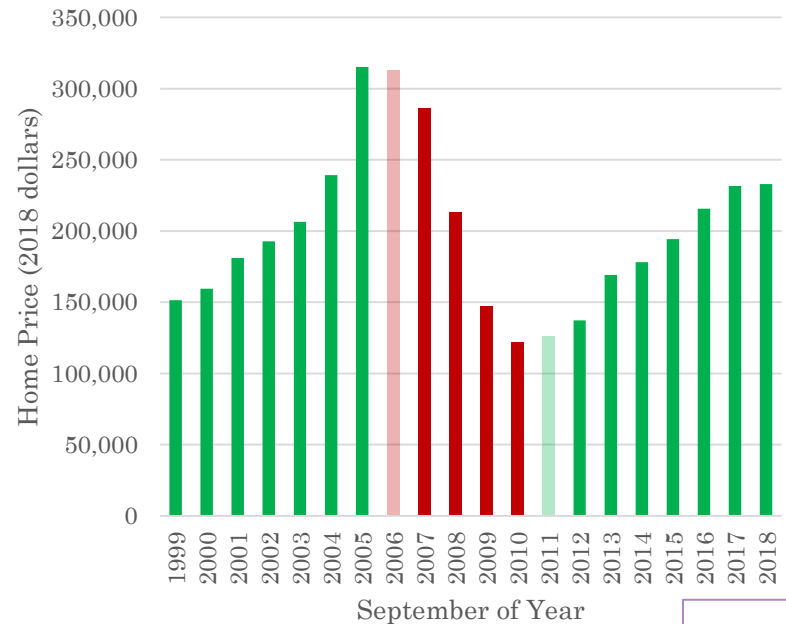
2.92 months of inventory in September 2018 indicates a seller's market in Orlando.

Given the tight supply of inventory in our market, home prices are expected to rise through 2020.

Orlando Housing Inventory
1997 - 2018



Median Home Prices in Orlando
Inflation-adjusted 1998-2018



The above prices are adjusted for inflation.
source: My Florida MLS
Last update: October, 2018

OUR 2018 HOUSING MARKET (5/5): HOUSING AFFORDABILITY INDEX

Orlando Home Affordability Index



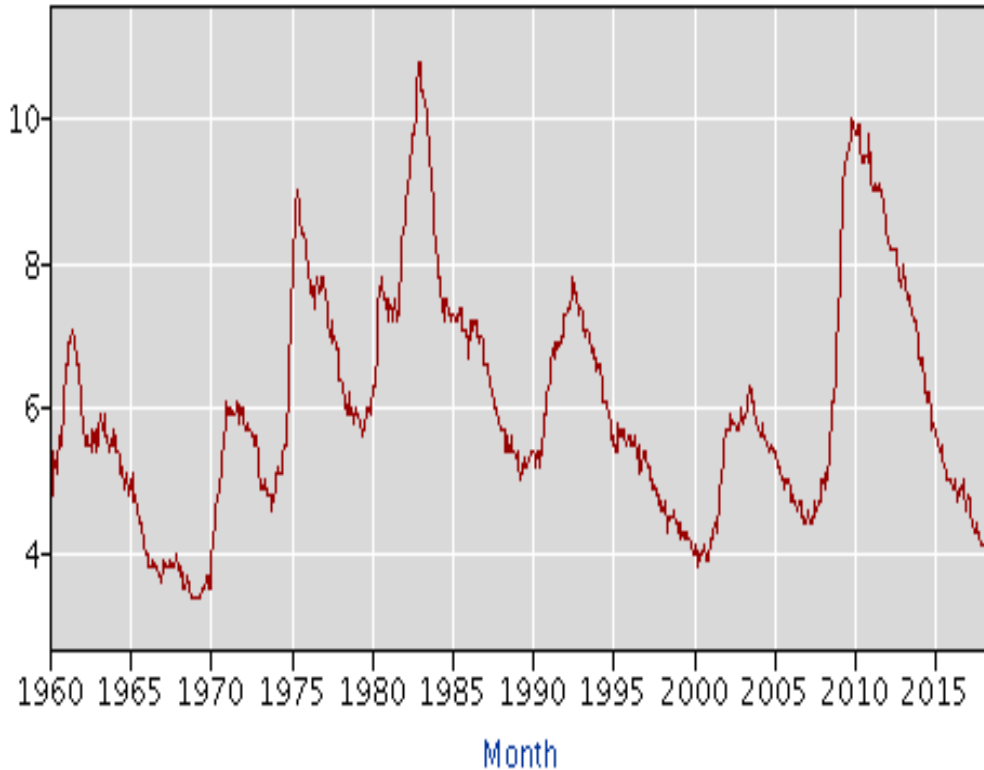
110% is our “warning mark” for this measure.
< 100% would indicate homes are overvalued.

<http://tinyurl.com/yd9mfgnt>

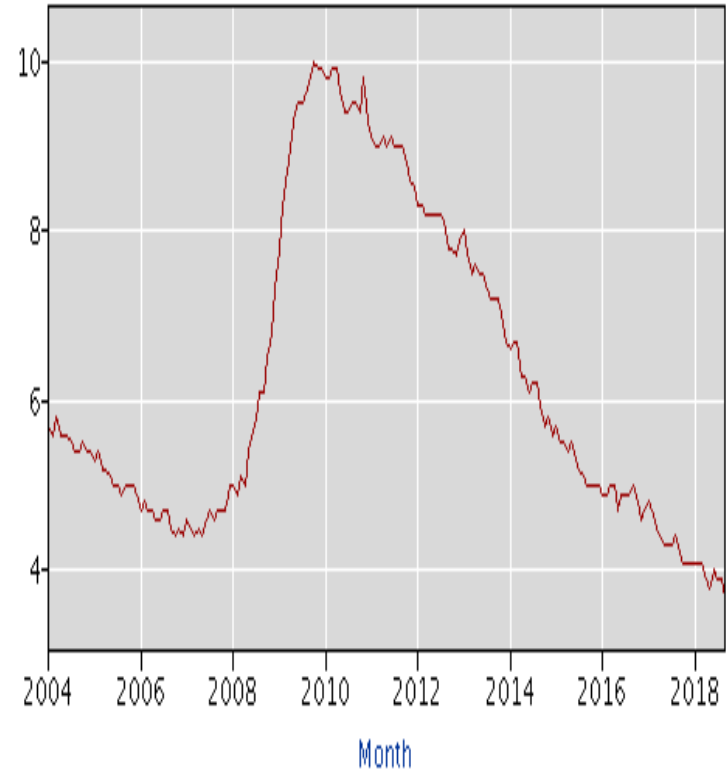
Last update: October, 2018

NATIONAL EMPLOYMENT SITUATION: UNEMPLOYMENT RATE (OFFICIAL U-3)

U.S. National Unemployment Rate,
1960 to 2018



U.S. National Unemployment Rate,
2004 to 2018



- U-3 includes those that are willing and able to work, and who have actively sought work in the past four weeks.
- It's not a perfect measure, but is useful for historical comparison.
- Currently, unemployment is near a 50 year low .
- Rising unemployment (month-to-month, year-over-year) occurs when a recession begins.

STATISTICS:

NATIONAL & ORLANDO

National	Sep-18	Sep-17	Sep-16	Dec-07	Dec-06
Employment to Population Ratio	60.4%	60.4%	59.7%	62.7%	63.4%
Unemployment Rate	3.7%	4.2%	5.0%	5.0%	4.4%
Wage Growth (nominal)	2.76%	2.83%	2.63%	3.75%	4.22%
Debt to GDP Ratio	104%	103%	104%	62.9%	61.7%
Orlando Real Estate				Dec-07	Dec-06
Interest Rate (30-Year Fixed)	4.63%	3.81%	3.46%	6.1%	6.14%
Median Home Value	\$233,000	\$231,718	\$215,619	\$286,113	\$313,044
Median Home Value Change from Previous Year	+ 1%	+ 7%	+ 11%	- 9%	- 1%
Months Supply of Inventory (LT Avg: 6)	2.93	3.39	3.33	22.58	10.04
Home Builder Confidence	69%	65%	68%	20%	39%
Orlando Home Affordability Index	127%	144%	162%	89.50%	119.80%

*Adjusted for Inflation. In 2018 dollars.

**Ratio based on 2017 GDP

SUMMARY OF LEADING INDICATORS

TO WATCH OUT FOR THE NEXT DOWNTURN IN ORLANDO METRO,
YOU MAY WANT TO KEEP THIS PAGE AT YOUR DESK.

General Economy

U-3 Unemployment

Jul-18	3.7%	Jul-17	4.3%
Aug-18	3.9%	Aug-17	4.4%
Sep-18	3.9%	Sep-17	4.2%

<http://tinyurl.com/zyq5xlx>

Watch for 3 consecutive months of rising unemployment over the same months of the previous year (see above comparison).
This will confirm the beginning of our next recession.

10Yr - 2Yr Treasury Yield

10/10/2018	0.34%
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<http://tinyurl.com/h9e4ljh>

Historically, an inversion of the 10 - 2 year treasury yield spread has preceded the past 5 recessions. This inversion occurs when the 2 year yield exceeds that of the 10 year.

Orlando Real Estate

Housing Affordability

Sep-18	127%
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<http://tinyurl.com/jfayp5s>

Housing Affordability gauges the stability of prices in our residential market. When this value falls below 110%, home values are overextended and likely to depreciate in the following 2-3 years.

Housing Inventory

Sep-18	2.92
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<http://tinyurl.com/jfayp5s>

Housing inventory is our key indicator for the residential market. In the coming years, look for the supply of homes to exceed 7 months supply. This will occur near the next peak in home prices.

Last updated: 10/12/2018

SOURCES

- Federal Reserve Bank of St. Louis (FRED)
- Federal Reserve Bank of New York
- Orlando Regional Realtors Association
- The U.S. Bureau of Labor Statistics
- The U.S. Bureau of Economic Analysis
- The U.S. Census Bureau
- The Congressional Budget Office
- My Florida Regional MLS
- FreddieMac
- Investopedia
- CNBC
- Economic Policy Institute
- Joe Keating, *May 1, 2018 Investment Strategy Statement*
- Dr. Sean Snaith- *University of Central Florida's Florida & Metro Economic Forecast, March 2018*
- Buyers Broker of Florida